

GFOA Study of Local Government Fragmentation

Summary of Preliminary Findings

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Local governments spent about \$1.9 trillion in 2017, collectively.ⁱ This was more than all 50 states put together, when we remove money passed through to local governments.ⁱⁱ While this might seem surprising at first, it might be less surprising when you consider that there are just over 90,000 units of local government in the United States,ⁱⁱⁱ providing services such as education, public safety, public health, infrastructure, and more.

Given the vast sums of money and number of governments involved, it is reasonable to ask: is there is too much **fragmentation** in local government and could public funds be better used if there was less fragmentation?

In this research, are exploring the following models for improving coordination of resources **between**¹ local governments:

- **Consolidation.** Combining multiple local governments into a single, larger unit.
- **Networked enterprises.** Creating formal and informal relationships between public, private, and non-profit organizations to better coordinate resources across the entire community.
- **Government as a platform.** Traditional government is a bureaucracy, where the departments of government are service providers. Government as a platform is about defining what the community needs and then “plugging in” the most effective service provider, regardless of whether it is private, non-profit, or another public organization.
- **Tax base sharing.** A fragmented local government system can result in certain local governments having a larger share of the tax base relative to their share of the population in the region, while other local governments have a much smaller share relative to their population. These fiscal disparities between local governments lead to disparate capacities to provide equitable public services. Tax base sharing seeks to correct that.

Before we examine each of the models above, we need to more precisely define the goals of our examination. If we are interested in the potential of these models to improve the use of resources, that improvement could happen along three basic dimensions:

- **Economize:** Less money is spent in total (assuming that too much was being spent before).
- **Efficiency:** The “per unit” cost of public services declines.
- **Value:** The benefit created by each dollar of public money spent goes up.

These three are not mutually exclusive, but it is useful to differentiate between them because each model may perform better or worse in each dimension.

¹ Coordination of resources within local governments is beyond scope of this paper. That topic is addressed in detail, using the Ostrom framework, in GFOA’s book *Financial Foundations for Thriving Communities*.

Government Consolidation

Given the similarity in services offered by different local governments in the same region, we can ask if consolidating those governments into larger units could result in better use of resources.

Consolidation is intended as a very direct solution to government fragmentation. However, there are two different types of fragmentation, each of which might respond differently to consolidation:

- **Horizontal fragmentation.** This when multiple governments in the same region provide a similar service. The most obvious example of this is when a region has multiple, separate municipal governments. This example implies that horizontally fragmented governments do not usually occupy the same geographic space. However, this is not always the case. Cities and their overlapping county government sometimes provide similar services.
- **Vertical fragmentation.** This refers to local governments providing different services. An example is where multiple special districts serve the same community (e.g., library district, park district, etc.), in addition to a general purpose municipal government. Vertical fragmentation implies at least some overlap in jurisdictional boundaries.

Here is what our research found about consolidation as a model for positively influencing efficiency, economies, and value in local government.

Consolidation of horizontally fragmented governments probably offers little to no net economization or efficiency benefits. The research suggests that consolidation of horizontally fragmented local governments has little potential to reduce costs.^{iv} Horizontally fragmented governments are associated with lower total spending (economization). This partially because the benefits of economies of scale are probably achieved at relatively small size for local government, so there is limited opportunity to reduce per unit costs (increase efficiency) with consolidation.^v Also, some evidence suggests that horizontally fragmented governments might monitor each other's tax rates and try to keep in line with their neighbors.^{vi} This force holds total spending down and this force would be weakened by consolidation.

The effect of consolidation on value is not clear. The research has no definitive answers on whether consolidation produces more benefit per dollar. Working against value is that a larger, consolidated government might be less responsive to the needs of the communities within its borders. For example, special interest groups are more likely to dominate public participation in larger governments.^{vii} In favor of value is that a larger, consolidated government might be able to provide more equitable services to the communities it serves. For example, if governments are consolidated, then a small local government couldn't capture a relatively "lucrative" commercial land use in its border and use the revenues to subsidize public services for its residents while the costs of commerce (traffic, etc.) impact the wider region.

Accentuate what works in horizontal fragmentation. Rather than incurring the costs of horizontal consolidation for dubious gains, policy makers would be better off accentuating the conditions associated with horizontal fragmentation that help hold down costs. For example, local governments already commonly develop local agreements to share resources. There is a lot more potential for local governments to engage in this kind of service sharing. We will examine this potential in detail in the next sections of this paper.

Beware the real cost of horizontal fragmentation. Horizontal fragmentation is not an unalloyed good thing for public finances. A real cost is urban sprawl. Urban planning policies are beyond the scope of this paper, but policy makers should recognize that by spreading population out over a wider area, the cost of public services is increased.^{viii}

Remove the conditions that encourage vertical fragmentation. Vertical fragmentation appears to be inefficient,^{ix} but it is difficult to recommend consolidation of vertically fragmented governments as a cost-beneficial strategy. This is because there has not been much research on the effects of this kind of consolidation. This is not to say that there aren't situations where this kind of consolidation would not work, but the research is not conclusive. However, it does seem safe to say that increasing numbers of vertically fragmented governments is not a good thing for overall efficiency of local government.

However, local officials are often actually *encouraged* to create special districts to meet local demand for public services that can't be met by municipal government. This is because of taxing, spending, or debt limitations imposed by state government inspire municipal officials to encourage the creation of special districts to get around the limitations. Hence, these state limits merely have the effect of shifting spending to vertically fragmented local governments.^x

Networked Enterprises

We just saw that local government consolidation probably has limited (or no) potential for positively influencing efficiency, economization, or value in local government. Consolidation is in, many ways, an industrial-age concept: taking two or more smaller bureaucracies and combing them into one larger bureaucracy. In this section we will begin to explore the potential of a model that epitomizes the information age: the network.

The challenges that communities face often cannot be addressed by a single government. A single local government may not have the authority, capacities, and/or resources that are needed. This is especially true as local governments contend with tighter budgets and more complicated problems like child literacy or drug addiction. A “networked enterprise” connects previously separate actors in the pursuit of a shared objective and multiply their collective power to achieve the objective. Networks are often closely associated with information technology—for example, a social media application like Facebook or a cryptocurrency like Bitcoin. Networks, however, do not have to exist purely as bits and bytes. The distributed and essentially free communication made available by modern information technology has given rise to the increasing prevalence of networked organizations in the physical world as well.

Many local governments are beginning to rely more on networked forms of organization to solve challenging community problems, *without growing* public budgets. Our research featured three cases of local governments that have formed successful networked enterprises.

- San Bernardino County in California articulated a shared vision for the entire county and enlisted organizations from many sectors in this vision, including many local governments within the county.
- The San Antonio Community Vision is remarkable for many reasons, including surviving three changes in mayoral leadership, extensive community participation, and getting results on issues that the community cares about.

- Battle Creek, Michigan, created a community vision called “BCvision”. It has brought together a number of public, private, and non-profit entities and has been positively received by local residents.

Here is what our research found about networked enterprises as a model for positively influencing efficiency, economies, and value in local government.

Networked enterprises can economize the size of local government. Networked enterprises attempt to improve the lives of community members by making a big impact on complicated issues like education, health and wellness, mobility and more. Clearly, a local government would have to vastly expand its taxing and spending in order to make a similar impact through a traditional, bureaucratic model.

Many observers of the United States government system have noted that the increasing dysfunction of the federal government is prompting state and, especially, local governments to step to the forefront in taking on the complicated, difficult problems that will make or break the livability of our communities.^{xi} Networked enterprises makes this possible while keeping local government affordable.

Networked enterprises can improve the perceived value of local government. A networked enterprise is anchored by a strong community vision. By definition, a strong community vision must reflect the will of the community. A networked enterprise aligns public, private, and non-profit resources with the vision, and, thereby, the will of the community. Thus, these resources would be producing more value, in the estimation of the public. BCVision has found some evidence of this through community surveys.^{xii} Also, the longevity of San Antonio’s Community Vision and the San Bernardino County networked enterprise suggests that the members of these networks find sufficient value in them to continue their participation.

That said, it would be reasonable to question how much of an impact these networks are making on issues like graduation rates, poverty, public health, etc., or if broader social and/or economic forces are responsible for much of the observed change. Unfortunately, the research does not exist to say. However, evidence-based policy making is becoming increasingly popular in local government as witnessed by the growth of databases and organizations that help local governments make evidence-based policy decisions. Certainly, a networked enterprise would make it easier to adopt strategies that are proven to work because the network could bring the necessary human and financial resource to bear.

Networked enterprises probably don’t have much impact on efficiency. A networked enterprise is not necessarily a replacement for traditional government. Bureaucracy has its advantages as well. Primarily, it can be more efficient and easier to manage in clear and predictable circumstances. Further, bureaucracy is known for stability, which can protect against disruption of important institutions. For example, the local governments featured in this paper still have day-to-day services run by traditionally configured county staff or contractors. The networked enterprises we have discussed have not been focused on the day-to-day services that make up the bulk of existing local government spending. Fortunately, a different and complementary networked model “Government as a Platform” can greatly improve efficiency, as we will see in the next section of this paper.

State policy makers can support the formation of networked enterprises. Networked enterprises have some common and well understood characteristics. State policy makers could support the capacity of local government to acquire these characteristics:

- *Help make available data needed for regular feedback on key indicators of community condition.* An important part of all three communities we studied was reporting on progress made towards the community vision by monitoring key indicators like poverty rates, child literacy, etc. State government could develop data clearing houses that make it easier for local governments to monitor these indicators. However, it would be inadvisable for state government to require local governments to monitor any particular indicators. The process of deciding what indicators are important is an indispensable part of putting together a community vision.
- *Provide training on skills to run a network.* States or quasi-state agencies often provide training programs for local officials. However, this training is typically focused on how to better manage a bureaucracy. In networked enterprise, local governments shifts from a “doer” to a “convener”. Being an effective convener requires a particular skill set that is different from managing a bureaucracy. For example, it requires:
 - Big-picture thinking, rather than narrow functional thinking.
 - Project management, rather than department management.
 - Establishing and monitoring outcomes, rather than controlling work processes.
 - Building coalitions, rather than relying on formal authority.
- *Provide support for evidence-based policy making.* State governments can begin to encourage local actors to use rigorous evidence on which policy interventions work and which don't. For example, some states have made rigorous evidence a requirement for local actors to obtain competitive grants from the state government.

Government as a Platform

Traditional government is a bureaucracy, where the departments of government provide day-to-day public services. Like networked enterprises, government as a platform is an information age model. It is about working with the community to determine collective goals and then “plugging in” the most effective service provider, regardless of whether it is the local government itself, a private, non-profit, or another public organization, or if it is an activity performed directly by the citizens themselves. This model is like the ubiquitous smart phone. A company like Google or Apple provides the platform and the best apps can be plugged in to accomplish the goals of the end user. Government as a platform differs from networked enterprises in that government as a platform is focused on optimizing day-to-day public services.

For example, the City of Englewood, Colorado and Washington County, Wisconsin have both extensively considered the potential to operate as a platform, rather than a traditional bureaucracy. This led Englewood to merge its fire protection services with the City of Denver. The new shared service saved Englewood about \$3 million annually or 33% of its original budget for the fire department. This is because Englewood was able to close one of its three fire stations as one of Denver's stations was sufficiently close to provide acceptable response times. Washington County formed a joint public health department with its neighbor, Ozaukee County. The shared public health department saved the counties a combined \$300,000 in annual operating costs in the first year.

Our research suggests a three-step process that local governments can use to enact the government as a platform model: 1) program inventory; 2) opportunity identification; 3) implementation. Let's examine each.

Program inventory. A program is a defined service like police patrol or tree services. This contrasts with the traditional approach of organizing by departments, like police and public works. A program is broader than a line item or task, but more detailed than a department. Programs are directly relevant to how people experience public services. Therefore, they are far more useful in a discussion about how to provide services, compared to departments and line items. A program inventory should include all programs in the government that provide a discrete service and which leads to an identifiable result or benefit. An inventory clarifies exactly what the government does.

Opportunity identification. In our case examples, this often proved as simple as convening participants from various local agencies around a table and comparing program inventories. For instance, Moffat County, in rural Montana, convened a meeting with Moffat County School District, the City of Craig, and Memorial Regional hospital. The County found that over half its budget was comprised of programs where at least one of the other organizations around the table had a comparable program. Other local governments that have done this have found even higher proportions. This is *not* to say that these are all duplicative services, but rather that there is a large area of opportunity to explore for partnerships, mergers, or insourcing/outourcing.

The City of Toledo, Ohio, undertook a similar process as Moffat County, but worked with the local chamber of commerce to look for opportunities to partner with the private sector. Some of the opportunities discovered include street sweeping and impound lots.

Implementation. Earlier, we showed how Englewood partnered with Denver to provide fire protection services. Fire services might be a big first step for many local governments. Moffat County, started with an easy opportunity. It was discovered that both the hospital and county jail had large laundry operations. The hospital found that its approach to laundry appeared to be far less cost-effective than the County's so it began shipping its laundry to the County, providing new revenue to the County.

Moving on from the three steps to government as a platform, here is what our research found about government as a platform as a model for positively influencing efficiency, economies, and value in local government.

Government as a platform can positively impact economization. Developing a program inventory helps a government decide what services it should or should not be in the business of providing. In a number of our case studies, governments identified services that it simply should no longer provide at all, in addition to services it could source differently.

Government as a platform can positively impact efficiency. Government as a platform helps local governments find more cost-effective ways to provide service, as our examples shown above described.

Government as a platform can positively impact value. Most fundamentally, the program inventory allows a government to closely align the services it provides (regardless of sourcing strategies) with community needs. This promotes value.

Further, government as a platform can help local governments realize economics of scale and other cost advantages *without* consolidation. We saw earlier that consolidation has a number of drawbacks that often outweigh the benefits, including the extreme complexity of making it happen and fierce resistance from the community due to concerns about losing their identity. Government as a platform avoids these problems. First, it doesn't attempt to merge or differently source services where there is no value in doing so. Consolidation, in contrast, merges all services regardless of value. Second, government as a platform allows governments to move at a pace they can accommodate. Englewood merged its fire operations because it was ready to. Moffat County started with a smaller scale change. Third, governments can avoid merging services that are core to its identity. For example, the City Manager of Littleton, Colorado, observed that utility billing could be good service to share with surrounding communities because there is no unique community character associated with what is an essentially a commoditized, back-office service. Allowing a community to maintain its identity is valuable.

Tax Base Sharing

One of the most important disadvantages of local government fragmentation are what are called "fiscal disparities" between local governments. The most well-known example of fiscal disparities is the disparity that arises between school districts. This happens when schools are funded primarily by local property taxes and some districts have an appreciably higher value of taxable property in their boundaries than other school districts. This is a problem because it will result in some children getting a materially worse education based on where they live.

The same basic problem can occur in municipal governments. This could be due to the value of taxable property in the jurisdiction relative to population. In states where sales taxes are an important revenue and are distributed to municipalities based on point-of-sale, a city that has a large shopping mall might get all of the revenue from the associated commerce even though residents of surrounding communities shop at the mall as well.

One of the most comprehensive and enduring solutions to fiscal disparities is found in the Twin Cities region in Minnesota. This tax-base sharing program spreads the fiscal benefits of commercial-industrial growth no matter where the property exists within the metro area. It reduces large differences in property tax wealth between communities with a lot of commercial-industrial tax base and those with little. Differences reflect how commercial-industrial development tends to concentrate near regional infrastructure and services, such as highways, wastewater treatment, and transit. Local taxing jurisdictions contribute 40% of growth in commercial, industrial, and public utility property tax base into an area-wide shared pool of tax base. Local property tax administrators distribute the shared pool of tax base. Communities with below-average property tax value per person receive a somewhat larger share of the area-wide tax base. Communities with above-average property tax value per person receive a somewhat smaller share of the area-wide tax base. This program was created in 1971 and has spurred a few other metro regions to try something similar around that time. There does not, however, appear to be any more recent attempts to create something similar.

A number of other, less comprehensive strategies could achieve at least some of the same benefits:

State revenue sharing. States can collect tax revenues where the taxes are generated proportionally or progressively relative to taxpayers' income or wealth. The revenues can then be distributed back to local governments based on some characteristic unrelated to taxpayer income/wealth. For example, a state

income tax would typically draw the most revenue from communities with wealthier residents, but could be distributed back to communities on a per capita basis.

Address development incentives. Development incentives provided by local governments are not often effective in achieving their goals.^{xiii} Incentives often simply cause firms to move within the region. This might change the relative tax receipts of local governments in the region, but create a net loss in the entire region.

End Notes

ⁱ Source: US Census Bureau. 2000, updated annually. Annual Survey of State and Local Government Finances, 1977-2017. Compiled by the State and Local Finance Data Query System. Washington, DC: Urban-Brookings Tax Policy Center. Data set accessed 28-Feb-20 02:08 PM at <https://slfdqs.taxpolicycenter.org>. This figure includes all sub-state governments, such as cities, counties, school districts, and special districts.

ⁱⁱ This figure includes direct expenditures only and not money passed through to local governments. Same source as footnote #1 above.

ⁱⁱⁱ 2012 Census of governments

^{iv} Goodman, Christopher B. "Local Government Fragmentation: What Do We Know?" *State and Local Government Review*. 51 (2): 134-144.

^v Joel Byrnes and Brian Dollery. "Do economies of scale exist in Australian local government? A review of the research evidence." *Urban Policy and Research* 20(4): 391-414. 2002.

^{vi} 2019 Nobel Prize winners Abhijit Banerjee and Esther Duflo give a modern take on this phenomena and relates it to 2009 Nobel Prize winner Elinor Ostrom's work in: Abhijit V. Banerjee and Esther Duflo. *Good Economics for Hard Times*. Public Affairs: New York. 2019. An Ostrom-inspired perspective on this issue in local government is available in: Spencer T. Brien. "Strategic Interaction Among Overlapping Local Jurisdictions." *American Review of Public Administration*. Vol 48(6). 584-595.

^{vii} Robert Bish. "Local Government Amalgamations: Discredited 19th Century Ideals Alive in the 21st." Toronto: C.D. Howe Institute. 2001.

^{viii} Goodman, Christopher B. "The Fiscal Impacts of Urban Sprawl: Evidence from US County Areas." *Public Budgeting and Finance*. Summer 2019

^{ix} *ibid*

^x Note the research seems to suggest that proliferation of special districts is related to constraints imposed on city government, but not county government. See: Christopher B. Goodman and Suzanne M. Leland. "Do Cities and Counties Attempt to Circumvent Changes in the Autonomy by Creating Special Districts?" *American Review of Public Administration*. 2018.

^{xi} Bruce Katz and Jeremy Nowak. *The New Localism: How Cities Can Thrive in the Age of Populism*. Brookings Institution Press. 2018.

^{xii} BCVision's surveys showed small, but notable improvements of resident perceptions in a number of areas that BCVision is intended to impact.

^{xiii} Timothy J. Bartik. *Making Sense of Incentives: Taming Business Incentives to Promote Prosperity*. (W.E. Upjohn Institute). 2019